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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

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ROBERT BURNS
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2013 JUL 2 PM 2 21

IN THE MATTER OF THE APPLICATION OF
FAR WEST WATER & SEWER, INC., AN
ARIZONA CORPORATION, FOR A
DETERMINATION OF THE CURRENT FAIR
VALUE OF ITS UTILITY PLANT AND
PROPERTY AND FOR INCREASES IN ITS
WASTEWATER RATES AND CHARGES
BASED THEREON FOR UTILITY SERVICE

DOCKET NO. WS-03478A-12-0307

REPLY BRIEF OF FAR WEST WATER AND SEWER, INC.

Arizona Corporation Commission
DOCKETED

JUL 02 2013

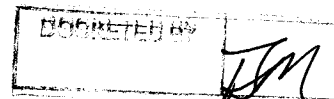


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1 **REPLY BRIEF OF FAR WEST WATER AND SEWER, INC.**

2 **I. REPLY TO STAFF**

3 Far West stands by its arguments in its initial brief.

4 **II. REPLY TO RUCO**

5 With one exception, Far West stands by its arguments in its initial brief. RUCO would
6 condition rate relief upon a resolution “of the discrepancy between the number of laterals and its
7 billing count.”¹ This is an immaterial issue. Neither RUCO nor any other party has identified
8 even one customer taking service during the test year that is not represented in the billing count.
9 And Mr. Jones testified that the lateral count—which is not used in ratemaking—improperly
10 included mobile home park tenants billed through a master meter, vacant subdivision where
11 laterals had been built but no homes were built, and other errors.² Far West also pledged to
12 investigate this issue and correct the lateral number.

13 RUCO’s trivial issue is hardly a reason to delay a hugely needed, long-delayed rate
14 increase.

15 **III. REPLY TO GILKEYS/RISTS**

16 **A. Introduction – Far West Has Served Its Sentence**

17 The Gilkeys and the Rists (“Intervenors”) largely rehash issues that were previously
18 considered by the Commission in 2009 (Docket No. WS-03478A-08-0868). In Decision No.
19 71447, the Commission considered most if not all of the issues Intervenors brought up in the
20 recent hearings. The Commission imposed one of most severe penalties ever imposed on an
21 Arizona utility, refusing to grant emergency rate relief, despite explicitly finding that Far West’s
22 Wastewater Division was insolvent.³ As a result, Far West has endured four years without rate
23 relief, yet has still fulfilled its public service obligations by investing millions of dollars in new
24 state-of-the-art wastewater treatment facilities, while continuing to provide quality customer
25 service.

¹ RUCO Brief at 18.

² Tr. at 953-56.

³ Decision No. 71447, page 22.

1 Far West has served its sentence, yet Intervenors want to continue punishment.
2 Intervenors give Far West no credit at all for staying the course, investing millions of dollars, and
3 improving customer service. None of Intervenors have any financial training. Yet, Intervenors
4 baselessly disparage Far West's books and records, ignore Staff's and RUCO's extensive
5 financial reviews, and disregard Levitzacks' thorough, independent financial audit for 2009,⁴ and
6 the subsequent independently reviewed financial statements for calendar years 2010 and 2011.⁵
7 Finally, Intervenors have not offered even one concrete improvement that an interim manager
8 could make or, more importantly, or suggested how an interim manager could improve Far
9 West's dire financial condition.

10 **B. Alleged Misdeeds by Previous Management Are Irrelevant**

11 Paragraphs a and b of the Intervenors' Brief concern alleged misdeeds by previous
12 management. As just discussed, the Commission has already dealt with these issues. Present
13 management has stepped up and served the Commission's sentence for past management
14 misdeeds, while still fulfilling their public service obligations by investing millions of dollars in
15 new state-of-the-art wastewater treatment facilities and providing quality customer service. Plant
16 construction practices in the 1990s and the tragic 2001 deaths are not relevant to this 2013 case.

17 **C. Present Management Is Qualified**

18 There is no evidence that present management is not qualified. Certainly, there was a
19 learning curve once the Capestros were forced to step in and take over control from Far West's
20 previous incompetent managers, but they have learned quickly and performed admirably.
21 Despite no emergency rate relief, they have stayed the course and completed Phase I of Far
22 West's wastewater improvement program.

23 Intervenors argue that the Capestros must be incompetent because they did not attend the
24 hearing. Besides being illogical, the argument is irrelevant. There is no Commission

⁴ Transcript at 785-87.

⁵ Transcript at 350:19-20.

1 requirement that company principals must testify or attend hearings. A company is allowed to
2 present its case however it desires.

3 Far West's witness, Ray Jones, was thoroughly prepared and was obviously intimately
4 knowledgeable concerning all issues relevant to this case. After multiple days on the stand,
5 Intervenors can only identify one issue that Mr. Jones was not able to discuss to their complete
6 satisfaction – the details of what capacity was available at the Section 14 plant when the Las
7 Barrancas and El Rancho Encantado subdivisions were connected to Far West's system
8 sometime before 2008.⁶ First, this obscure issue, if it really is an issue, is irrelevant to a 2013
9 rate case based on a 2011 test year. Second, Intervenors do not explain why they did not ask
10 these questions in discovery, if they really cared about the alleged issue. Third, despite their
11 failure to conduct proper discovery, they still could have asked Mr. Jones to research the issue
12 and provide a post-hearing exhibit to resolve it.

13 Although it is not relevant, no one even asked why the Capestros were not at the
14 hearings. The Capestros planned to attend the hearing and paid in advance for a hotel room in
15 Phoenix during the hearings. Unfortunately, Paula Capestro required gynecological surgery in
16 San Diego on April 10, and was subsequently instructed to rest as much as possible and not to
17 return to work until May 1.⁷ Mr. Capestro spent much of that time attending to his wife at their
18 San Diego home while he worked from home. The Capestros were forced to forfeit their
19 payment for a hotel room in Phoenix during the hearings.

20 Finally, undersigned counsel was under no obligation to accept service for Mr. Capestro.

21 **D. Service Quality Has Been Satisfactory**

22 Intervenors identified no issues with meter reading, billing, or similar service issues.
23 Further, Staff engineering witness Jian Liu independently investigated Far West's service quality
24 and concluded that there were no "complaints recorded in the service quality category since 2010

⁶ Although Las Barrancas was "connected," there were no homes constructed there as of the test year. Tr. at 102.

⁷ See Exhibit A.

1 and the number of Complaints is trending downward.”⁸ Finally, based on his investigation and
2 his site visits, Mr. Liu concluded:

3 Based on the reports provided by the Commission Consumer Services Section and the
4 ADEQ, and the physical inspection, there is no evidence to demonstrate that Company
5 has violated the Quality of Service Statute.⁹

6 The retirement of the Palm Shadows treatment plant has resolved most odor issues. Now,
7 virtually all remaining odor issues concern Far West’s Marwood Plant. First, it is important to
8 note that there were no odor issues with the plant during visits by Staff or RUCO.¹⁰ Subsequent
9 odor issues were largely a result of an illegal acetone dump that killed all the bacteria in the
10 digester.¹¹ Further, Far West’s proposed new 40th Street Lift Station should reduce flows to
11 Marwood and make odor issues much less likely.¹²

12 **E. Sewage Spills Are Not at an Unusual Level**

13 Intervenor’s state: “Mr. Jones has testified that the number of spills is higher than should
14 be expected,” citing transcript page 1018. There is no such testimony anywhere on page 1018 or
15 elsewhere. The only negative “testimony” concerning spills came from the questioner, Mr. Rist.
16 At page 1019, Judge Nodes cautioned: “Mr. Rist, you are essentially testifying at this point.”
17 Even Mr. Rist did not “testify that the number of spills is higher than should be expected. He
18 conceded that only three spills in 2012 were even reportable under normal circumstances.”¹³

19 Intervenor’s have conducted no studies to benchmark Far West’s number of spills against
20 what is typical for Arizona wastewater utilities. Certainly, three reportable spills in one year do
21 not seem excessive and Intervenor’s have offered no evidence to suggest otherwise.

⁸ Hearing Exhibit S-2, Surrebuttal Testimony of Jian Liu at 3:18-19.

⁹ *Id.* at 4:13-15.

¹⁰ Staff, see *id.* RUCO witnesses visited the plants and did not reference any odor issues. See Exhibit RUCO-9, Direct Testimony of Royce A. Duffett, at 3.

¹¹ Transcript at 650-51.

¹² Transcript at 1004-05. This lift station was sometimes referred to as the Paula Street lift Station. Transcript at 927-28.

¹³ Transcript at 1018:18-19.

1 **F. Customers Are Not Bearing the Burden of a Failed Plant**

2 First, contrary to Intervenor's allegations, "rate payers" have not paid for Palm Shadows.
3 Customers have never paid for the plant because it was contributed by the developer.¹⁴ Further,
4 Mr. Jones testified extensively that the Palm Shadows capacity would have had to be replaced
5 with a larger facility such as Section 14—regardless of its performance—as part of normal
6 system consolidation to accommodate Far West's dramatic growth.¹⁵ This would have required
7 construction of the Palm Shadows force main, even if Palm Shadows had continued to operate as
8 it did for many years after it entered service.

9 **G. Far West's Operations Are Transparent**

10 Intervenors allege without evidence that Far West's operations are somehow not
11 transparent. Far West files all reports required by its regulators and has provided all information
12 required for this rate case, including responses to hundreds of data requests. Intervenors do not
13 identify even one instance where Far West has refused to provide relevant information.

14 Intervenors also believe that they should be allowed to visit treatment plants at any time.
15 Intervenors ignore the significant individual safety issues of allowing unfettered access to
16 treatment plants. And it is certainly naïve to believe in this day and age that it would be in the
17 public interest for Far West to allow unsupervised access to its facilities.

18 **H. Far West Complies to the Best of Its Ability with All Commission and ADEQ**
19 **Requirements.**

20 The only thing preventing Far West from full regulatory compliance is money. Each
21 month Far West must balance revenues against expenses, including overdue payments to long-
22 standing creditors. There simply is not enough money to pay salaries, purchased water,
23 purchased power, existing loan repayments, and other large expenses, and to pay Spartan Homes,

¹⁴ Transcript at 205.

¹⁵ Transcript at 311-14; 942-948.

1 for example.¹⁶ Only a rate increase will allow Far West to begin to catch up with past
2 obligations such as to Spartan Homes.¹⁷

3 **I. Far West Is Trying to Obtain Necessary Easements**

4 Mr. Jones testified that Far West has been attempting since 2010 to obtain the easements
5 needed to close the Del Rey and Villa Royale treatment plants.¹⁸ Intervenors have offered no
6 suggestions as to how Far West could expedite these efforts.

7 **J. Far West's Affiliate Dealings Have Not Hurt Customers**

8 Staff thoroughly investigated Far West's affiliate dealings and concluded that "ratepayers
9 were not harmed."¹⁹ In further response to Intervenors concerning this issue, please see Staff's
10 Opening Brief, pages 13-17.

11 It is also very important to note that Far West would have been unable to continue
12 operations without the willingness of affiliates to provide funds.

13 Without the availability of these short-term loans from affiliates to pay normal operating
14 expenses such as salary, rent, electricity, and supplies, Far West would have failed. The
15 affiliates were the only source of funds to keep an insolvent company operating. If these
16 companies had not been affiliated, these funds would not have been available. Again, no
17 bank or company will voluntarily lend to an insolvent company.²⁰

18 Based on this evidence, the important conclusion is that customers have actually benefitted from
19 the affiliate transactions.

20 **K. Equity Cannot Be Infused until Some Time after New Rates Go Into Effect**

21 In the United States, business owners cannot be forced to continue to invest in an
22 insolvent company. Nevertheless, the Capestros have continued to invest, both personally and

¹⁶ On March 30, 2012, Far West asked the Commission (Docket No. WS-03478A-08-0256) to delay payment to Spartan Homes until 90 days after new rates go into effect. The Commission has not acted on this request.

¹⁷ As discussed in its Initial Brief, Far West has reluctantly agreed to satisfy its obligation to Spartan Homes before new rates go into effect. However, this will require robbing Peter to pay Paul. Other creditors will have to suffer further delayed payments.

¹⁸ Transcript at 1040.

¹⁹ Exhibit S-8, Rate Design Supplemental Testimony of Gerald Becker, at 6:14.

²⁰ Transcript at 17:13-20.

1 through affiliates, in Far West. In 2009, Far West shareholders infused \$3,097,354 of equity into
2 the Company and since then have pledged personal assets as security for Company debt.²¹

3 Unfortunately, annual net losses have continued and will continue to erode equity until
4 new rates have been in effect for some time. At that point, a third party may be willing to invest
5 in Far West, but only if Far West's financial condition has become strong enough to earn a
6 reasonable return on the investment. We are presently far away from that possibility.

7 **L. Far West Has Applied for Approval of a Hook-Up Fee Tariff**

8 Far West filed for approval of water and wastewater hook-up fee tariffs on June 19, 2013,
9 in Docket No. WS-03478A-13-0200. Far West is requesting hook-up fees beginning at \$2,000
10 each for new water and wastewater connections.

11 **M. There Is No Reason to Appoint an Interim Manager**

12 Intervenor ask the Commission to order appointment of an interim manager. Far West
13 discussed why this request was unwarranted in its Brief.²² Staff also agrees that there is no
14 present reason to appoint an interim manager.²³

15 **N. There Is No Reason for a Forensic Audit**

16 Intervenor ask the Commission to order that a forensic audit be conducted. In its Initial
17 Brief, Far West discussed why this request was unwarranted.²⁴ Intervenor's so-called reasons for
18 such an appointment are baseless.

19 Intervenor allege that an improperly labeled \$25,000 cash disbursement supports their
20 position. As Exhibit Gilkey-16 shows, Far West admitted its error and corrected it. This tiny
21 error, made by an analyst when responding to a data request, hardly supports conducting an
22 expensive and time-intensive forensic audit. What is important is that the books and records
23 were correct, and Far West was able to provide, directly from its accounting system, extensive

²¹ Exhibit A-2, Rebuttal Testimony of Ray Jones, at 25:21-22.

²² Far West Brief at 20-21.

²³ Staff Brief at 11-13.

²⁴ Far West Brief at 21-22.

1 detail documenting the purpose of the payment, including the specific H&S invoices paid by this
2 cash disbursement. Far West further demonstrated that the payment had no ratemaking impact in
3 this case. Far West's books and records were complete and accurate. This is persuasive
4 evidence that a forensic audit is not needed.

5 Intervenor also point to an alleged \$12,500 "discrepancy between cash disbursements
6 and the 1099 issued to Andrew Capestro."²⁵ As evidence they cite Exhibit Gilkey-14. However,
7 Gilkey 14 completely reconciled the alleged discrepancy.

8 Intervenor also rely on their identification of an RV Park that had not been previously
9 listed as such. This was not an accounting issue, but a disagreement concerning appropriate rate
10 design. This is not an issue that an auditor would even investigate.

11 After Mr. Jones reviewed the issue, he agreed with Intervenor and reclassified the
12 facility as an RV Park.

13 There is one commercial business, the Schechert Family Aquatics & Fitness Center,
14 located in the Manufactured Housing Subdivision (MHS-20) zoning district that has
15 characteristics sufficiently similar to an RV Park that charging the RV Park rate may be
16 appropriate here, even though it is not a traditional RV Park. The Fitness Center is a
17 health and fitness club that also rents RV spaces. There are 49 RV spaces on the
18 property, of which 48 are available for rental. Since the Fitness Center is not in the RVP
19 zoning district and not a traditional RV Park, Far West has been billing the facility under
20 its Commercial tariff. ... I recommend that the facility be billed for 48 RV spaces.²⁶

21 This is typical of normal, good-faith disagreements during the rate case process. An applicant
22 files a case. In turn, Staff, RUCO, and other parties review the application. They may accept,
23 modify, or disagree with the applicant's positions on rate base, income, cost-of-capital, rate
24 design, or other issues. The applicant may then accept the other party's position or ask the
25 Commission to decide the issue. In this case, Far West evaluated Intervenor's position
26 concerning how the fitness center should be treated for rate-design purposes, researched the
27 issue, and then agreed with Intervenor. This is exactly how the process is supposed to work.
28 Far West's response is further evidence that a forensic audit is not needed.

²⁵ Intervenor's Brief at 8:11-12.

²⁶ Exhibit A-3, Rate Design Rebuttal Testimony of Ray Jones, at 8.

1 Finally, Intervenor's try to make something out of the fact that two notes were supposedly
2 not examined. Again, this is hardly evidence supporting a forensic audit. If there were an entry
3 for a liability and no note to support that liability, then Intervenor's might have an issue, but this
4 is not the case. Further, the Schechert Family Trust Demand Note was the subject of extensive
5 discovery and testimony.²⁷ Staff and RUCO, the parties with financial training who actually
6 investigated Far West's books and records, found no issues concerning this note.

7 **O. An "Independent" Board of Directors Is Unwarranted**

8 Far West is a private company with two shareholders. There are no allegations or
9 evidence that it does not comply with Arizona's requirements for corporate governance,
10 including its present board of directors.

11 Intervenor's want to replace the existing board of directors with an "independent" board
12 of directors. This board would presumably have authority over how to spend Far West's funds
13 and invest its capital. This type of takeover would obviously be prohibited by the Takings
14 Clauses of both the U.S. and Arizona Constitutions.

15 **IV. REPLY TO SPARTAN HOMES**

16 Spartan Homes "asks that the Commission order Far West to demonstrate compliance
17 with all Commission statutes, rules and decisions before the company is permitted to implement
18 any rate increase approved in this docket."²⁸ This request is improper. First, no company could
19 make this demonstration. Spartan Homes is essentially asking Far West to prove that is not
20 violating any Commission statutes, rules, and decisions before it can receive rate relief. This
21 impossible condition has never been imposed on any company and would violate Far West's
22 constitutional right to earn a return on the fair value of its property. Further, until rate relief has
23 been provided, Far West cannot comply with all known obligations under the Commission's
24 statutes, rules, and decisions. This fundamental fact supported the stipulated conditions

²⁷ Exhibit Gilkey-7; Exhibit S-11; Transcript 1051-54.

²⁸ Spartan Homes Brief at 2.

1 recommended by the Staff and Far West. Some conditions must be satisfied pre-rate relief; some
2 must await rate relief.

3 Spartan Homes also asks that Far West be current with all refunds of advances in aid of
4 construction before rate relief can be provided.²⁹ Spartan Homes is asking Far West to create
5 money out of thin air. The evidence is clear that there simply is not enough money to pay
6 salaries, purchased water, purchased power, existing loan repayments, and other large expenses
7 until rate relief is provided. Adding another expense as a precondition for rate relief would just
8 set up Far West for certain failure.

9 **V. CONCLUSION**

10 Nothing in the other parties' briefs should alter the Commission's conclusion that Far
11 West has justified the relief requested in its Initial Brief and Final Schedules.

12 **Respectfully submitted** on July 2, 2013, by:

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14 
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²⁹ *Id.* at 3.

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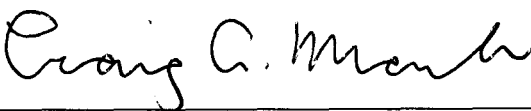
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Exhibit A

April 19, 2013

To Whom It May Concern:

On the following date(s) 4/10/13 - 4/30/13

Our Patient: Paula Capestro

Is under a doctor's care and unable to: Push, Pull, Carry or Lift more than 8 pounds. She has been instructed to rest as much as possible until her follow up examination by MD on 4/30/13. It is preferable that she not work during this time.

If applicable: Patient will be able to return to work on: 5/1/13.

Thank you,

A handwritten signature in black ink, appearing to read 'Cynthia', followed by a stylized flourish or second name.

Cynthia Parbury, MA